MULTIMEDIA UNIVERSITY

STUDENT IDENTIFICATION NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

T1, 2018/ 2019

BEM7064 – ECONOMICS FOR MANAGERS
(All Sections/ Groups)

28 SEPTEMBER 2018
9.00 a.m – 12.00 p.m
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This question paper consist of **FIVE (5)** pages (including the cover page).

2. Answer **ALL** questions. The marks distributions are given in parentheses.

3. Write all your answers in the **Answer Booklet** provided.

QUESTION ONE (20 MARKS)

(a) The following are some costs incurred by a shoe manufacturer. Evaluate and decide whether each one is a fixed cost, variable cost or has some element of both.

- (i) The cost of leather to make shoes.
- (ii) The fee paid to an advertising agency
- (iii) Electricity for lighting
- (iv) Electricity for running the machines.
- (v) Basic minimum wages agreed with the union of workers.

(10 marks)

(b) Justify why normal profits are regarded as a cost (and included in the cost curves) in the study of economics.

(5 marks)

(c) Assess **TWO (2)** business activities of a large department store that are likely to experience economies of scale?

(5 marks)

QUESTION TWO (20 MARKS)

A **perfectly competitive** firm faces a price of **RM14 per unit**. It has the following short-run cost schedule:

Table 1

Output	Total Cost (TC) (RM)	Average Cost (AC) (RM)	Marginal Cost (MC) (RM)	Total Revenue (TR) (RM)	Marginal Revenue (MR) (RM)
0	10	--		--	
1	18				
2	24				
3	30				
4	38				
5	50				
6	66				
7	91				
8	120				

Continued...

(a) Copy **Table 1** into your answer booklet. Calculate the Average Cost (AC), Marginal Cost (MC), Total Revenue (TR), and Marginal Revenue (MR) at each level of output. (Enter the figures for MC and MR in the space between each column.)

(10 marks)

(b) Plot the Average Cost (AC), Marginal Cost (MC), and Marginal Revenue (MR) curve on a diagram.

(5 marks)

(c) On the graph drawn for Question 2(b), mark the profit-maximising output and label that point as Π. What is profit-maximising output quantity?

(2 marks)

(c) How much (supernormal) profit is made at this output? Indicate the profit area in the graph drawn for Question 2(b).

(3 marks)

QUESTION THREE (20 MARKS)

(a) Assess firms in monopolistic competition in comparison to firms in the perfectly competitive market.

(12 marks)

(b) Justify why oligopoly may be more disadvantageous for consumers than monopoly.

(8 marks)

QUESTION FOUR (20 MARKS)

(a) Explain why an increase in injections will lead to a multiplied rise in national income.

(6 marks)

(b) Defend why the *AD* curve is usually downward sloping.

(6 marks)

(c) Explain why is it difficult to use fiscal policy to 'fine tune' the economy?

(8 marks)

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CASE STUDY (20 MARKS)

Disinflation in Europe and Japan: An erosion of market power?

The rise of a low inflation environment

Compared to their US and Japanese rivals, European businesses used to have a reputation for raising prices to make more profits. In an economic environment where inflation was endemic, business could easily hide from its inefficiencies and adopt this short-term strategy.

However, following the recession of the early 1990s – Europe's worst recession since the war – attitudes and practices seem to have changed, and potentially for the better. European business seemed to be adopting a more competitive way of doing business. The result, especially in the early 2000s, when demand was growing relatively slowly again, was that prices fell in many sectors.

This process was known as 'disinflation'. It resulted largely from changes in the external business environment. Here slow growth, financial restraint by central banks attempting to keep inflation within limits, and fierce global competition led many firms to question whether price rises are necessary or justifiable.

One of the main sources of competition was from low-cost countries, such as China and India. Cheap imports from these countries put downward pressure on competing industries in Europe. What is more, outsourcing call-centre, back-office and IT work to developing countries put downward pressure on wages. This downward effect on prices and wages has been dubbed the 'China price' effect.

Japanese business found itself in a very similar position to many European countries. It too experienced a lengthy recession, in which prices fell as businesses tried to shift unwanted stocks. In addition, the high value of the yen and the subsequent reduction in the cost of imports stimulated a huge rise in foreign competition, which succeeded in forcing prices down yet further.

The benefits of disinflation

Are general reductions in prices a good thing or a bad thing? The answer to this largely depends upon whether you are a consumer or producer, whether you are looking at the short or long term, and whether any price reduction is met by higher productivity gains and not redundancies.

In the short term, consumers will clearly benefit from lower prices: in effect, their real income will rise (assuming no corresponding fall in wages). Over the longer term, both producers and consumers are likely to gain as lower underlying rates of inflation enable governments to reduce interest rates. For business this means cheaper capital and greater opportunities for investment and growth.

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The down side to disinflation is whether it can be achieved without a massive impact upon levels of income and employment. If businesses simply respond to lower prices, and hence profit margins, by making workers redundant, income levels may begin to fall, stimulating a downward spiral of demand. Thus the key to successful disinflation is to offset falling prices with greater efficiency. Those firms unable to meet these new stringent efficiency goals will not be able to generate profits from higher prices, and will invariably become ripe for takeover by those that can.

Extracted from: Sloman, J., & Garratt, D. (2016). 'Disinflation in Europe and Japan: An erosion of market power?' *Essentials of Economics* (7th Edition). Harlow: Pearson Education Limited.

(a) Summarise the external business environment factors that lead to 'disinflation' in Europe and Japan.

(8 marks)

(b) Appraise whether there are 'gainers' and 'losers' during disinflation.

(8 marks)

(c) What are the new strategies that businesses have been forced to adopt in order to maintain profits in a low-inflation economy

(4 marks)

End of Paper